

Mason County Central School District

**FINANCIAL STATEMENTS
AND REPORT OF INDEPENDENT
CERTIFIED PUBLIC ACCOUNTANTS**

June 30, 2008

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MASON COUNTY CENTRAL SCHOOLS

Management's Discussion and Analysis For Fiscal Year Ended June 30, 2008

Mason County Central Schools is a K-12 school district located in Mason, Lake and Oceana Counties, Michigan. The Management's Discussion and Analysis, a requirement of GASB 34, is intended to be the Mason County Central Schools Administration's discussion and analysis of the financial results for the fiscal year ended June 30, 2008. Please read in conjunction with the district's financial statements following this section.

Generally accepted accounting principles ("GAAP") according to GASB 34 requires the reporting of two types of financial statements: District Wide Financial Statements (full accrual) and Fund Financial Statements (modified accrual).

Fund Financial Statements

The fund financial statements are reported on a modified accrual basis, which means that only assets that are measurable and currently available are reported, as well as liabilities that can expect to be paid with current financial resources. They provide detailed information about the most significant funds.

The fund statements comply with the legal requirements of the Michigan Department of Education's School Accounting Manual. The General Fund reports activities for the district's major instructional and instructional support activities. Additional governmental funds are Capital Projects, Debt and School Service, which report food service and athletic activities.

The fund financial statements report capital assets as expenditures during the current period rather than as an asset on the balance sheet. When debt is issued the proceeds are reported as a resource rather than as a liability on the balance sheet. The current year principal payments are reported as expenditures rather than reductions in liabilities.

District Wide Financial Statements

The district wide statements are reported on a full accrual basis and help to measure the financial health of the district as a whole. This means that all of the District's assets and liabilities, both short and long term are reported using accounting methods similar to those of private sector companies. All revenues and expenditures are reported regardless of when cash is received or paid. Capital assets and long-term obligations are reported in the Statement of Net Assets. A reconciliation is provided to identify the differences between governmental activities (reported in the statement of net assets and the statement of activities) and the fund financial statements.

Management's Discussion and Analysis For Fiscal Year Ended June 30, 2008 - Continued

The composition of the financial report is as follows:

Management's Discussion and Analysis (MD & A)
(Required Supplemental Information)

Basic Financial Statements

District-wide Financial Statements Fund Financial Statements

Notes to the Basic Financial Statements

Budgetary Information for the General Fund
(Required Supplemental Information)

Combining Financial Statements of Non-Major Funds
Other Supplemental Information

Fiduciary Fund

The school district holds fiduciary responsibility for the student activity funds held in its care. These fiduciary activities are reported on a separate statement of net assets. The district cannot use these assets to finance its operations, but is responsible for ensuring that the assets held in these funds are used for their intended purpose.

Management's Discussion and Analysis For Fiscal Year Ended June 30, 2008 - Continued

Summary of Net Assets (provides a perspective of the School District as a whole)

| | <u>June 30, 2007</u> | <u>June 30, 2008</u> | <u>Percentage Chg</u> |
|----------------------------------------------------|----------------------|----------------------|-----------------------|
| Assets | | | |
| Current assets | <u>\$15,072,005</u> | <u>\$ 5,242,909</u> | <u>(65.2)%</u> |
| Noncurrent assets | <u>-</u> | <u>494,669</u> | <u>100.00%</u> |
| Capital assets | 23,156,756 | 29,338,944 | 26.7% |
| Less: Accumulated depreciation | <u>(8,496,965)</u> | <u>(9,000,094)</u> | <u>5.9%</u> |
| Capital assets, net book value | <u>14,659,791</u> | 20,338,850 | 38.7% |
| Total assets | <u>\$29,731,796</u> | <u>\$26,076,428</u> | <u>(12.3)%</u> |
| Liabilities | | | |
| Current liabilities | \$ 8,286,386 | \$ 4,781,812 | (42.3)% |
| Long-term liabilities | <u>20,605,116</u> | <u>19,830,508</u> | <u>(3.8)%</u> |
| Total liabilities | <u>\$28,891,502</u> | <u>\$24,612,320</u> | <u>(14.8)%</u> |
| Net Assets | | | |
| Invested in capital assets, net of related debt | (6,310,542) | 20,513 | 100.3% |
| Restricted | 7,250,982 | 1,457,486 | (79.9)% |
| Unrestricted | <u>(100,146)</u> | <u>(13,891)</u> | <u>86.1%</u> |
| Total net assets | <u>840,294</u> | <u>1,464,108</u> | <u>74.2%</u> |
| Total liabilities and net assets | <u>\$29,731,796</u> | <u>\$26,076,428</u> | <u>(12.3)%</u> |

Management's Discussion and Analysis For Fiscal Year Ended June 30, 2008 - Continued

The analysis above focuses on the net assets of the district while the change in these net assets is discussed below. The district's improved financial position is the result of many factors. The School District's net assets were \$840,294 at June 30, 2007 and \$1,464,108 at June 30, 2008. Current assets decreased by \$9,829,096 in 2008 reflecting use of cash for the construction project. Correspondingly, capital assets increased by \$6,182,188 also reflecting the new building project. Current liabilities decreased by \$3,504,574 reflecting near completion of the construction project. Capital assets, net of related debt, increased 100.3 percent. This figure reports the original cost, less depreciation of capital assets minus long term debt used to finance these acquisitions. The increase of \$6,331,055 is due to asset acquisitions less depreciation expense exceeding new debt minus principal payments. Most of the debt will be repaid from voter-approved property taxes assessed as debt payments come due. Restricted assets are reported separately to indicate legislative requirements and debt covenants. These assets may not be used by the District in its day-to-day operations. \$(100,146) and \$(13,891) of net assets is unrestricted in 2007 and 2008, respectively. This figure represents the accumulated results of all past years' operations. Year to year variances in these assets are significantly affected by General Fund operations.

Statement of Activities (provides the results of operations of the School District as a whole)

| | <u>June 30, 2007</u> | <u>June 30, 2008</u> | <u>Percentage Chg</u> |
|--------------------------------|----------------------|----------------------|-----------------------|
| Revenues | | | |
| General Revenues: | | | |
| Property taxes | \$ 3,002,287 | \$ 3,146,094 | 4.8% |
| State unrestricted foundation | 9,180,233 | 9,053,329 | (1.4)% |
| Other | 914,434 | 274,039 | (70.0)% |
| Program Revenues: | | | |
| Charges for services | 566,332 | 593,601 | 4.8% |
| Operating grants/contributions | 3,066,398 | 3,022,340 | (1.4)% |
| Total revenues | <u>\$16,729,684</u> | <u>\$16,089,403</u> | (3.8)% |
| Expenditures: | | | |
| Instruction | 8,820,820 | 8,825,055 | 0.1% |
| Support services | 4,520,636 | 4,414,047 | (2.4)% |
| Food service | 719,418 | 703,274 | (2.2)% |
| Athletic | 301,647 | 285,721 | (5.3)% |
| Interest on long-term debt | 759,127 | 734,363 | (3.3)% |
| Depreciation | <u>390,335</u> | <u>503,129</u> | 28.9% |
| Total expenditures | <u>\$15,511,983</u> | <u>\$15,465,589</u> | (0.3)% |
| Change in net assets | 1,217,701 | 623,814 | (48.8)% |
| Net assets-beginning of year | <u>(377,407)</u> | <u>840,294</u> | |
| Net assets-end of year | <u>\$ 840,294</u> | <u>\$ 1,464,108</u> | |

Management's Discussion and Analysis For Fiscal Year Ended June 30, 2008- Continued

- Total actual revenues were under budget by \$84,186 and total actual expenditures were under by \$103,734. Actual fund balance at June 30 was within \$21,059 of budgeted fund balance; which is approximately 1.5% of budgeted expenditures.

Capital Assets

At June 30, 2008 the District has \$29,338,944 invested in capital assets including land, buildings, furniture, vehicles and equipment summarized as follows:

| | <u>Balance</u> <u>June 30, 2007</u> | <u>Additions</u> | <u>Deletions</u> | <u>Balance</u> <u>June 30, 2008</u> |
|--------------------------------|----------------------------------------|--------------------|------------------|----------------------------------------|
| Capital Assets | \$23,156,756 | \$6,182,188 | \$ - | \$29,338,944 |
| Less: Accumulated Depreciation | <u>(8,496,965)</u> | <u>(503,129)</u> | <u>-</u> | <u>(9,000,094)</u> |
| Net Investment Capital Outlay | <u>\$14,659,791</u> | <u>\$5,679,059</u> | <u>\$ -</u> | <u>\$20,338,850</u> |

The District's major capital additions this year consisted of construction projects.

Debt

A summary of bonded indebtedness follows:

| <u>Balance</u> <u>June 30, 2007</u> | <u>New Debt</u> | <u>Payments</u> | <u>Balance</u> <u>June 30, 2008</u> |
|----------------------------------------|-----------------|--------------------|----------------------------------------|
| <u>\$20,621,742</u> | \$ - | <u>\$(630,000)</u> | <u>\$19,991,742</u> |

The other obligation is employee-compensated absences that is presented in more detail in the notes to the financial statements along with unamortized bond refinancing costs.

Currently Known Facts, Conditions and Decisions

The State foundation revenue is calculated by multiplying the District's blended student count by the current year foundation allowance. The blended count for the 2008/09 school year is 25% of the February, 2008 student count and 75% of the September, 2008 student count. Since State foundation revenue accounts for 66% of the District's total General Fund revenue, student count is a critical component affecting the budget. The budget for 2008/09 adopted in June, 2008 was based on an estimate of 20 fewer students to be counted in September. The overall national, state and local economic declines have compelled the District to use a conservative estimate of student count.

Management's Discussion and Analysis For Fiscal Year Ended June 30, 2008- Continued

The cost of all of the District's activities this year stayed approximately the same at \$15,465,589. Correspondingly, the District's total revenues decreased by 3.8% to \$16,089,403. This decrease is attributed in great part to a decrease in state foundation payments reflecting a decrease in the number of students; and a decrease in Other reflecting a decrease in investment income reflective of the reduced cash balances in the capital projects funds available to invest. In 2008, some activities were partially funded by those who benefited from the programs in the amount of \$593,601 or by governmental subsidies of \$3,022,340. The difference between these two figures and the total of the District's expenditures of \$15,465,589 is \$11,849,648. This clearly points out the significant reliance placed on State unrestricted resources of \$9,053,329 and local taxpayers' dollars of \$3,146,094 to fund the District's activities. Consequently, the Board of Education and Administration must annually evaluate the needs of the District to balance with available unrestricted funding.

The school district experienced an increase of \$623,814 in net assets. This was primarily due to an increase in net capital assets due to the building project. The difference between the change in net assets and the change in fund balance is provided in a reconciliation in the financial statements.

The District's Funds

As of June 30, 2008 the combined governmental funds reported a fund balance of \$1,817,992 or a decrease of \$5,781,049 over last year.

- General Fund reported a decrease of \$10,672 to \$262,924.
- Debt Funds showed an increase of \$269,443 to \$944,147 reflecting the additional deposit to the QZAB account. Millage rates are reviewed annually to ensure the District assesses enough taxes to pay the annual bond-related debt costs. These taxes can only be used to pay debt service obligations.
- The special revenue fund balance decreased by \$17,715 to \$38,933.
- The Capital Projects Funds reflect a decrease of \$6,022,105 due to the activity of the ongoing construction project.

General Fund Budget Highlights

Throughout the school year, the District monitors and revises its budget to account for continual changes in revenues and expenditures. The Uniform Budget Act of the State of Michigan requires that the Board of Education adopt a budget for the upcoming school year prior to July 1, which is the start of the new fiscal year. Budget revisions are formally adopted in October, March and June. As part of the required supplemental information, a schedule showing original and final budget amounts compared to those actually received and paid is part of the financial statements. Variances were as follows:

- State program revenues final budget increased by \$60,336 over the original budget primarily due to an increase in student and higher foundation amount than what was originally budgeted.. Local and intermediate sources increased by \$96,262 reflecting higher than originally budgeted tax and local program revenues. Incoming transfers and other transactions increased by \$98,207 over the original budget to reflect an Act 18 transfer from Mason-Lake ISD. The expenditure final budget side increased by \$337,967 reflecting contract settlements with the district's labor groups.

Management's Discussion and Analysis For Fiscal Year Ended June 30, 2008 - Continued

The District used an estimated foundation amount of \$7,300 in calculating state revenues for the 2008/09 budget. Once the final student count and per pupil funding is formalized, State law requires the District to amend its budget if revenues plus fund balance are not sufficient to fund original appropriations.

The budget for 2008/09 basically maintains supply line items at the same level as 2007/08. The district had four veteran teachers retire June 30, 2008 and will recall the teacher on layoff and replace the other positions with beginning level teachers.

The district will finalize construction activity as the building project funded with the successful passage of a bond proposal in February, 2006 comes to an end. The completion date for final projects is scheduled to be November, 2008.

Contacting the School District's Financial Management

This financial report is designed to provide the School District's citizens, taxpayers, customers, investors and creditors with a general overview of the School District's finances and to reflect accountability for the money it receives. If you have questions about this report or need additional information, contact the Central Business Office, 300 W. Broadway, Scottville, MI 49454.



DENNIS, GARTLAND & NIERGARTH

Business and Financial Advisors
Our clients' success is our business

Thomas J. Westberg, CPA
Frank R. Gartland, CPA
James W. Niergarth, CPA
Robert J. Schneider, CPA
Michael L. Niergarth, CPA
Mary J. Gartland, CPA
Eric J. K. Schneider, CPA
Lisa M. Niergarth, CPA

REPORT OF INDEPENDENT CERTIFIED PUBLIC ACCOUNTANTS

Board of Education
Mason County Central School District

We have audited the accompanying financial statements of the governmental activities, each major fund and the aggregate remaining fund information of the *Mason County Central School District* (the "School District") as of and for the year ended June 30, 2008, which collectively comprise the School District's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the School District's management. Our responsibility is to express opinions on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinions.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, each major fund and the aggregate remaining fund information of the Mason County Central School District as of June 30, 2008 and the respective changes in financial position thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated September 19, 2008 on our consideration of the School District's internal control over financial reporting and our tests of its compliance with certain provisions, laws, regulations, contracts and grant agreements, and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and important for assessing the results of our audit.

Member of



415 Munson Avenue, Post Office Box 947
Traverse City, Michigan 49685-0947
931 946 1722, FAX: 231 946 2762
www.dgncpa.com

The management's discussion and analysis on pages i - vii and the budgetary comparison information on page 23, are not a required part of the basic financial statements but are supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the supplementary information. However, we did not audit the information and express no opinion on it.

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the School District's basic financial statements. The combining financial statements of non-major governmental funds on pages 24 and 25 and the Schedule of Expenditures of Federal Awards on pages 27 and 28, which is required by U.S. Office of Management and Budget Circular A-133, *Audits of State, Local and Government and Non-Profit Organizations*, are presented for purposes of additional analysis and are not a required part of the financial statements of the School District. Such information has been subjected to the auditing procedures applied during the audit of the basic financial statements and, in our opinion, is fairly stated in all material respects in relation to the financial statements taken as a whole.

Dennis. Gartland & Niergarth

September 19, 2008

Mason County Central School District

STATEMENT OF NET ASSETS

June 30, 2008

| | <u>Governmental Activities</u> |
|-------------------------------------------------|------------------------------------|
| ASSETS | |
| Current assets | |
| Cash and cash equivalents | \$ 2,598,399 |
| Investments | 389 |
| Due from other governments | 2,474,347 |
| Taxes receivable | 33,414 |
| Other receivables | 14,243 |
| Inventory | <u>122,117</u> |
| Total current assets | <u>5,242,909</u> |
| Non-current assets | |
| Restricted cash | 952 |
| Restricted investments | 493,717 |
| Capital assets, net of accumulated depreciation | <u>20,338,850</u> |
| Total non-current assets | <u>20,833,519</u> |
| Total assets | <u><u>\$ 26,076,428</u></u> |
| LIABILITIES AND NET ASSETS | |
| LIABILITIES | |
| Current liabilities | |
| Accounts payable | \$ 80,874 |
| State aid note payable | 2,350,000 |
| Salaries payable and related expenses | 1,397,610 |
| Other accrued expenses | 180,956 |
| Current portion of long-term obligations | <u>772,372</u> |
| Total current liabilities | 4,781,812 |
| Non-current portion of long-term obligations | <u>19,830,508</u> |
| Total liabilities | <u>24,612,320</u> |
| NET ASSETS | |
| Invested in capital assets, net of related debt | 20,513 |
| Restricted | |
| Debt Service | 820,879 |
| Capital Improvements | 571,988 |
| School-based activities | 39,619 |
| Future unemployment | 25,000 |
| Unrestricted (deficit) | <u>(13,891)</u> |
| Total net assets | <u>1,464,108</u> |
| Total liabilities and net assets | <u><u>\$ 26,076,428</u></u> |

The accompanying notes are an integral part of these statements.

Mason County Central School District

STATEMENT OF ACTIVITIES

Year Ended June 30, 2008

| Functions/Programs | Expenses | Program Revenues | | Net (Expense)/Revenue and Changes in Net Assets |
|---------------------------------|---------------|----------------------|------------------------------------|-------------------------------------------------|
| | | Charges for Services | Operating Grants and Contributions | |
| Governmental activities | | | | Governmental Activities |
| Instruction | \$ 8,825,055 | \$ 46,291 | \$ 2,029,334 | \$ (6,749,430) |
| Supporting Services | 4,414,047 | 157,777 | 642,280 | (3,613,990) |
| Food Service | 703,274 | 334,351 | 350,426 | (18,497) |
| Athletics | 285,721 | 55,182 | 300 | (230,239) |
| Interest on long-term debt | 734,363 | - | - | (734,363) |
| Depreciation - unallocated* | 503,129 | - | - | (503,129) |
| Total governmental activities | \$ 15,465,589 | \$ 593,601 | \$ 3,022,340 | (11,849,648) |
| General purpose revenues | | | | |
| Property taxes | | | | |
| Levied for general purposes | | | | 1,652,007 |
| Levied for debt service | | | | 1,494,087 |
| State school aid - unrestricted | | | | 9,053,329 |
| Investment and other | | | | 274,039 |
| Total general purpose revenues | | | | 12,473,462 |
| Change in net assets | | | | 623,814 |
| Net assets - beginning of year | | | | 840,294 |
| Net assets - end of year | | | | \$ 1,464,108 |

* See Note D

The accompanying notes are an integral part of these financial statements.

Mason County Central School District
BALANCE SHEET - GOVERNMENTAL FUNDS

June 30, 2008

| | General Fund | Capital Projects Fund A | Capital Projects Fund B QZAB | Other Governmental Funds | Total Governmental Funds |
|---------------------------------------|---------------------|-------------------------------|------------------------------------|--------------------------------|--------------------------------|
| ASSETS | | | | | |
| Cash and cash equivalents | \$ 1,530,007 | \$ 392,221 | \$ 225,648 | \$ 450,523 | \$ 2,598,399 |
| Investments | - | 389 | - | - | 389 |
| Due from other governments | 2,455,855 | - | - | 18,492 | 2,474,347 |
| Other receivables | 11,382 | - | - | 2,861 | 14,243 |
| Due from other funds | 16,738 | - | 800 | 6,582 | 24,120 |
| Inventories - supplies and materials | 74,139 | - | - | 47,978 | 122,117 |
| Restricted cash | - | - | - | 952 | 952 |
| Restricted investments | - | - | - | 493,717 | 493,717 |
| Total assets | <u>\$ 4,088,121</u> | <u>\$ 392,610</u> | <u>\$ 226,448</u> | <u>\$ 1,021,105</u> | <u>\$ 5,728,284</u> |
| LIABILITIES AND FUND BALANCES | | | | | |
| LIABILITIES | | | | | |
| Accounts payable and accrued expenses | \$ 1,475,197 | \$ 43,756 | \$ 2,514 | \$ 14,705 | \$ 1,536,172 |
| Due to other funds | - | 800 | - | 23,320 | 24,120 |
| State aid anticipation note payable | 2,350,000 | - | - | - | 2,350,000 |
| Total liabilities | <u>3,825,197</u> | <u>44,556</u> | <u>2,514</u> | <u>38,025</u> | <u>3,910,292</u> |
| FUND BALANCES | | | | | |
| Reserved for Debt Service | - | - | - | 944,147 | 944,147 |
| Reserved for future unemployment | 25,000 | - | - | - | 25,000 |
| Reserved for capital improvements | - | 348,054 | 223,934 | - | 571,988 |
| Reserved for adult ed | 686 | - | - | - | 686 |
| Reserved for inventories | 74,139 | - | - | 38,933 | 113,072 |
| Unreserved | | | | | |
| General Fund | 163,099 | - | - | - | 163,099 |
| Total fund balances | <u>262,924</u> | <u>348,054</u> | <u>223,934</u> | <u>983,080</u> | <u>1,817,992</u> |
| Total liabilities and fund balances | <u>\$ 4,088,121</u> | <u>\$ 392,610</u> | <u>\$ 226,448</u> | <u>\$ 1,021,105</u> | |

Reconciliation of Governmental Fund Balances to District-Wide Government Activities Net Assets

Amounts reported for governmental activities in the statement of net assets are different because:

Capital assets used in governmental activities are not financial resources and, therefore, are not reported as assets in governmental funds. The cost of the assets is \$29,338,944 and the accumulated depreciation is \$9,000,094. 20,338,850

Property taxes receivable will be collected in the next fiscal year, but are not available soon enough to pay for the current period's expenditures and, therefore, are not reported as assets in the funds. 33,414

Long-term liabilities, including bonds payable, are not due and payable in the current period and, therefore, are not reported as liabilities in the funds. Long-term liabilities at year-end consist of:

| | | |
|------------------------------------|--------------|--------------|
| Bonds payable | \$19,991,742 | |
| Unamortized bond refinancing costs | (314,101) | |
| Accrued interest on the bonds | 123,268 | |
| Unamortized bond premium | 640,696 | |
| Accumulated leave liability | 284,543 | (20,726,148) |

Total net assets - governmental activities \$ 1,464,108

The accompanying notes are an integral part of these financial statements.

Mason County Central School District

STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES - GOVERNMENTAL FUNDS

Year Ended June 30, 2008

| | General Fund | Capital Projects Fund A | Capital Projects Fund B QZAB | Other Governmental Funds | Total Governmental Funds |
|--------------------------------------------------------------------------------------|-------------------|-------------------------------|------------------------------------|--------------------------------|--------------------------------|
| Revenues | | | | | |
| Property taxes | \$1,646,563 | \$ - | \$ - | \$ 1,491,173 | \$ 3,137,736 |
| Interest | 48,801 | 111,333 | 51,642 | 22,644 | 234,420 |
| State revenues | 10,111,432 | - | - | 31,437 | 10,142,869 |
| Federal revenues | 653,432 | - | - | 318,989 | 972,421 |
| Other | 1,203,766 | - | - | 389,833 | 1,593,599 |
| Total revenues | <u>13,663,994</u> | <u>111,333</u> | <u>51,642</u> | <u>2,254,076</u> | <u>16,081,045</u> |
| Expenditures | | | | | |
| Instruction | 8,886,991 | - | - | - | 8,886,991 |
| Supporting Services | 4,410,305 | - | - | - | 4,410,305 |
| Food Service | - | - | - | 703,274 | 703,274 |
| Athletics | - | - | - | 285,721 | 285,721 |
| Debt Service | | | | | |
| Principal | - | - | - | 630,000 | 630,000 |
| Interest | - | - | - | 759,873 | 759,873 |
| Other | - | 2,692 | 200 | 850 | 3,742 |
| Capital outlay | - | 3,899,250 | 2,282,938 | - | 6,182,188 |
| Total expenditures | <u>13,297,296</u> | <u>3,901,942</u> | <u>2,283,138</u> | <u>2,379,718</u> | <u>21,862,094</u> |
| REVENUES OVER (UNDER) EXPENDITURES | <u>366,698</u> | <u>(3,790,609)</u> | <u>(2,231,496)</u> | <u>(125,642)</u> | <u>(5,781,049)</u> |
| Other financing sources (uses) | | | | | |
| Operating transfers in | - | - | - | 377,370 | 377,370 |
| Operating transfers out | <u>(377,370)</u> | <u>-</u> | <u>-</u> | <u>-</u> | <u>(377,370)</u> |
| Total other financing sources (uses) | <u>(377,370)</u> | <u>-</u> | <u>-</u> | <u>377,370</u> | <u>-</u> |
| REVENUES (UNDER) OVER EXPENDITURES AND OTHER FINANCING SOURCES (USES) | <u>(10,672)</u> | <u>(3,790,609)</u> | <u>(2,231,496)</u> | <u>251,728</u> | <u>(5,781,049)</u> |
| Fund balance, beginning of year | <u>273,596</u> | <u>4,138,663</u> | <u>2,455,430</u> | <u>731,352</u> | <u>7,599,041</u> |
| Fund balance, end of year | <u>\$ 262,924</u> | <u>\$ 348,054</u> | <u>\$ 223,934</u> | <u>\$ 983,080</u> | <u>\$ 1,817,992</u> |

The accompanying notes are an integral part of these financial statements.

Mason County Central School District

RECONCILIATION OF THE GOVERNMENTAL FUNDS STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES WITH THE DISTRICT-WIDE STATEMENT OF ACTIVITIES

Year Ended June 30, 2008

Total net change in fund balances - governmental funds **\$ (5,781,049)**

Amounts reported for governmental activities in the statement of activities are different because:

Capital outlays to purchase or build capital assets are reported in the governmental funds as expenditures. However, for governmental activities those costs are shown in the statement and allocated over their estimated useful lives as annual depreciation expenses in the statement of activities. This is the amount by which capital outlays exceed depreciation in the period.

| | | |
|----------------------|------------------|-----------|
| Capital outlays | \$6,182,188 | |
| Depreciation expense | <u>(503,129)</u> | 5,679,059 |

Because some property taxes will not be collected for several months after the School District's fiscal year-end, they are not considered as "available" revenues in the governmental funds; they are however, recorded as revenues in the statement of activities. This is the amount by which current year uncollected property taxes exceed prior year collected taxes in the period.

8,358

In the statement of activities, certain operating expenses - compensated absences - are measured by the amounts earned during the year. In the governmental funds, however, expenditures for these items are measured by the amount of financial resources used (essentially, the amounts actually paid). This year, compensated absences earned were less than amounts paid by \$9,436. Accumulated termination pay earned was less than amounts paid by \$52,500.

61,936

Repayment of bond principal (including refunding) is an expenditure in the governmental funds, but it reduces long-term liabilities in the statement of net assets and does not affect the statement of activities.

630,000

Amortization of deferred refunding costs.

(30,104)

Amortization of deferred bond premium.

52,100

Interest on long-term debt in the statement of activities differs from the amount reported in the governmental funds because interest is recorded as an expenditure in the funds when it is due, and thus requires the use of current financial resources. In the statement of activities, however, interest expense is recognized as the interest accrues, regardless of when it is due. The greater amount of interest reported in the statement of activities is the net result of the increase in accrued interest on bonds payable.

3,514

Change in net assets of governmental activities

\$ 623,814

Mason County Central School District

STATEMENT OF FIDUCIARY NET ASSETS

June 30, 2008

| | <u>Agency Fund</u> |
|---------------------------|------------------------------|
| ASSETS | |
| Cash and cash equivalents | \$ 354,235 |
| Accounts receivable | <u>6,719</u> |
| Total assets | <u><u>\$ 360,954</u></u> |
| LIABILITIES | |
| Accounts payable | \$ 4,273 |
| Due to student groups | <u>356,681</u> |
| Total liabilities | <u><u>\$ 360,954</u></u> |

Mason County Central School District

NOTES TO FINANCIAL STATEMENTS

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Introduction

Mason County Central School District (the "School District") is a Michigan public school district consisting of two elementary schools, a middle school, high school and early childhood center. The School District primarily serves portions of Oceana, Lake and Mason Counties. As of June 30, 2008, the School District employed 102 professional staff and 125 non-professional staff and had 1530 students enrolled within its School District.

The accounting policies of the School District conform to generally accepted accounting principles as applicable to governments. The School District is considered to be a local government unit.

The accounting and reporting framework and the more significant accounting principles and practices of Mason County Central School District are discussed in subsequent sections of this note. The remainder of the notes are organized to provide explanations, including required disclosures, of the School District's financial activities for the fiscal year ended June 30, 2008.

The Financial Reporting Entity

Mason County Central School District's Board of Education (the "Board") is the basic level of government which has oversight responsibility and control over all activities related to the public school education. The Board receives funding from local, State and Federal governmental sources and must comply with the concomitant requirements of these funding source entities. However, the Board is not included in any other governmental "reporting entity" as defined in GASB pronouncements, since Board members are elected by the public and have decision-making authority to levy taxes, the power to designate management, the ability to significantly influence operations and primary accountability for fiscal matters. In addition, under the criteria of the GASB pronouncements, student, parent and teacher organizations are not included, except to the extent that the schools hold assets in the capacity of an agent.

Government-Wide and Fund Financial Statements

Government-Wide Financial Statements

The statement of net assets and statement of activities display information about the School District as a whole, except for its fiduciary activities. Individual funds are not displayed.

NOTES TO FINANCIAL STATEMENTS - Continued

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

The statement of activities reports the expenses of a given function offset by program revenues directly connected with the functional program. A function is an assembly of similar activities and may include portions of a fund or summarize more than one fund to capture the expenses and program revenues associated with a distinct functional activity. Program revenues include: (1) charges for services which report fees, fines and forfeitures, and other charges to users of the School District's services; (2) operating grants and contributions which finance annual operating activities including restricted investment income; and (3) capital grants and contributions which fund the acquisition, construction or rehabilitation of capital assets. These revenues are subject to externally imposed restrictions to these program uses. Taxes and other revenue sources not properly included with program revenues are reported as general revenues.

Fund Financial Statements

The balance sheet and statement of revenues, expenditures and changes in fund balances (i.e., fund financial statements) for the School District's governmental funds are presented after the government-wide statements. These statements display information about major funds individually and non-major funds in the aggregate for governmental funds. Major funds are generally those that represent 10% or more of governmental fund assets, liabilities, revenues or expenditures.

Measurement Focus, Basis of Accounting and Financial Statement Presentation

The financial statements of the School District are prepared in accordance with generally accepted accounting principles ("GAAP"). The School District's reporting entity applies all relevant Governmental Accounting Standards Board ("GASB") pronouncements and applicable Financial Accounting Standards Board ("FASB") pronouncements and Accounting Principles Board ("APB") opinions issued on or before November 30, 1989, unless they conflict with GASB pronouncements. The School District's reporting entity does not apply FASB pronouncements or APB opinions issued after November 30, 1989.

The government-wide statements report using the economic resources measurement focus and the accrual basis of accounting generally including the reclassification or elimination of internal activity (between or within funds). Reimbursements are reported as reductions to expenses. Fiduciary fund financial statements also report using this same focus and basis of accounting, although internal activity is not eliminated in these statements. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Property taxes are recognized in the year for which they are levied while grants are recognized when grantor eligibility requirements are met.

Governmental fund financial statements report using the current financial resources measurement focus and the modified accrual basis of accounting. Revenues are recognized when they are both measurable and available. Available means collectible within the current period or soon enough thereafter to pay current liabilities. The School District considers revenues to be available if they are collected within 60 days of the end of the fiscal year. Expenditures are recorded when the related fund liability is incurred, except for general obligation bond principal and interest which are reported as expenditures in the year due.

NOTES TO FINANCIAL STATEMENTS - Continued

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

Major revenue sources susceptible to accrual include property taxes, intergovernmental revenues and investment income. In general, other revenues are recognized when cash is received.

Fund Types and Major Funds

Activities in Major Funds

The General Fund is the general operating fund of the School District. It is used to account for all financial resources except those required to be accounted for in another fund.

The Capital Projects Funds are used to account for financial resources to be used for the acquisition or construction of major facilities. The major Capital Projects Funds used by the School District are the Fund A and Fund B QZAB.

Other Governmental Funds

The Special Revenue Funds are used to account for the proceeds of specific revenue sources that are legally restricted to expenditures for special purposes. The Food Service and Athletic Funds are accounted for as Special Revenue Funds.

The Debt Service Funds are used to account for the accumulation of resources for, and the payment of, bond principal, interest and related costs.

Fiduciary Funds

The Agency Fund accounts for assets held by the School District as an agent for individuals, private organizations, other governments or other funds. Agency Funds are custodial in nature (assets equal liabilities) and do not involve measurements of results of operations. The Student Activity Fund is an Agency Fund.

Cash and Equivalents

The School District's reporting entity considers highly liquid investments (including restricted assets) with an original maturity of three months or less when purchased to be cash equivalents.

Investments

Investments are reported at fair value which is determined using selected bases. Short-term investments are reported at cost, which approximates fair value.

Inventories

Inventories in governmental funds consist of expendable supplies held for consumption stated on a first-in, first-out basis. They are reported at cost, which is recorded as an expenditure at the time individual inventory items are used.

NOTES TO FINANCIAL STATEMENTS - Continued

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

Capital Assets

Capital assets are recorded at cost or, if donated, the fair value at the time of donation. Capital assets are depreciated over their estimated useful lives ranging from 5 to 40 years. The School District generally capitalizes assets with cost of \$5,000 or more as purchase and construction outlays occur. No depreciation is recorded on land. Expenditures for major renewals and betterments that extend the useful lives of the capital assets are capitalized. Expenditures for maintenance and repairs are charged to current expenditures as incurred. Depreciation is computed using the straight-line method. When capital assets are disposed, the cost and applicable accumulated depreciation are removed from the respective accounts and the resulting gain or loss is recorded in operations.

Estimated useful lives, in years, for depreciable assets are as follows:

| | |
|------------------------------------|-------------|
| Buildings | 30-40 years |
| Improvements, other than buildings | 15-20 years |
| Vehicles | 8 years |
| Furniture, machinery and equipment | 5-20 years |

Long-Term Debt, Deferred Debt Expense and Bond Discounts/Premiums

In the government-wide financial statements, outstanding debt is reported as a liability. Bond issuances costs, bond discounts or premiums, and the difference between the reacquisition price and the net carrying value of refunded debt are capitalized and amortized over the terms of the respective bonds using a method that approximates the effective interest method.

The governmental fund financial statements recognize the proceeds of debt and premiums as other financing sources of the current period. Issuance costs are reported as expenditures.

Fund Equity

The governmental fund financial statements report reserved fund balances for amounts not available for appropriation or legally restricted for specified purposes.

Program Revenues

Program revenues derive directly from the program itself or from outside parties for the restricted use in a particular program. On the statement of activities, program revenues reduce the net cost of the various functions to reflect the amount which is financed from the School District's general revenues.

The School District's most significant program revenues are Title I, At-Risk and School Lunch Programs, which are reported as operating grants and contributions.

Spending Policy

The School District's policy is to apply restricted revenues first when an expense is incurred for purposes when both restricted and unrestricted net assets are available.

NOTES TO FINANCIAL STATEMENTS - Continued

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

Encumbrance Accounting

The School District formally records encumbrances in the accounting records during the year as a normal practice. In accordance with generally accepted accounting principles, outstanding encumbrances at year-end for which goods or services are received are reclassified as expenditures and accounts payable. All other encumbrances in the annual budgeted funds are reversed at year-end and are either canceled or are included as reappropriations of fund balance for the subsequent year.

Allocation of Expenses

The School District reports each function's direct expenses, those that are specifically associated with a service, program or department and, thus, are clearly identifiable to a particular function.

The School District has elected to not allocate indirect expenses.

Use of Estimates in the Preparation of Financial Statements

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual amounts could differ from those estimates.

NOTE B - CASH AND INVESTMENTS

Bank Deposits

At June 30, 2008, the School District's cash and investments include the following:

| | <u>Balance Sheet Classification</u> | | |
|--------------------------------------|-------------------------------------|--------------------|--------------|
| | <u>Cash and Equivalents</u> | <u>Investments</u> | <u>Total</u> |
| Bank deposits and cash on hand | \$1,331,118 | \$ - | \$1,331,118 |
| Investments in financial institution | | | |
| pooled funds | 1,622,468 | - | 1,622,468 |
| Investments | - | 494,106 | 494,106 |
| | \$2,953,586 | \$494,106 | \$3,447,692 |

Cash of all the funds of the School District is on deposit with financial institutions which provide FDIC insurance coverage, or in highly liquid pooled money funds.

Custodial Credit Risk - Deposits

In the event of a bank failure, the School District's deposits may not be returned to it. As of June 30, 2008, \$1,350,129 of the School District's bank balance of \$1,481,399 was exposed to custodial risk because it was uninsured and uncollateralized.

NOTES TO FINANCIAL STATEMENTS - Continued

NOTE B - CASH AND INVESTMENTS - Continued

Investments

| <u>Investment Type</u> | <u>Fair Value</u> | <u>Investment Maturities (in years)</u> | | | |
|---------------------------------------|--------------------|-----------------------------------------|-------------|-------------|---------------------|
| | | <u>Current</u> | <u>1-5</u> | <u>6-10</u> | <u>More than 10</u> |
| Financial institution pooled funds | \$1,622,468 | \$1,622,468 | \$ - | \$ - | \$ - |
| U.S. Government Issues | <u>494,106</u> | <u>494,106</u> | <u>-</u> | <u>-</u> | <u>-</u> |
| | <u>\$2,116,574</u> | <u>\$2,116,574</u> | <u>\$ -</u> | <u>\$ -</u> | <u>\$ -</u> |

Interest Rate Risk

In accordance with the School District's investment policy, the School District will minimize interest rate risk, which is the risk that the market value of securities in the portfolio will fall due to changes in market interest rates by structuring the investment portfolio so that securities mature to meet cash requirements for ongoing operations, thereby avoiding the need to sell securities in the open market and investing operating funds primarily in short-term securities and limiting the average maturity in accordance with the School District's cash requirements.

Credit Risk

State law limits investments in commercial paper and corporate bonds to a prime or better rating issued by nationally recognized rating organizations. The School District's investment policy further limits its investment choices to investments considered to be "low-risk". The investments in financial institution pooled funds were unrated at June 30, 2008.

NOTE C - RECEIVABLES, UNCOLLECTIBLE ACCOUNTS AND DEFERRED REVENUE

Property Taxes Receivable, Deferred Revenue and Property Tax Calendar

Property taxes are levied, billed and attached as enforceable liens in July of the School District's fiscal year. Townships within the School District collect and remit taxes until February 15, at which time the uncollected real property taxes are turned over to the counties as delinquent. Delinquent real property taxes are funded by the county and remitted to the School District. Delinquent personal property tax remains a receivable until collected from the taxpayer by the townships and remitted to the School District. In the governmental fund financial statements, if delinquent taxes are not paid within 60 days of year-end, they are recorded as deferred revenue. In the government-wide financial statements, property taxes receivable and related revenue include all amounts due the School District regardless of when cash is received. Over time, substantially all property taxes are collected.

During the fiscal year, \$16.6780 per \$1,000 of equalized non-homestead property value of \$99,053,059 was levied for general operating purposes. For debt service purposes, \$5.80 per \$1,000 of equalized homestead and non-homestead property value of \$257,601,284 was levied.

NOTES TO FINANCIAL STATEMENTS - Continued

NOTE C - RECEIVABLES, UNCOLLECTIBLE ACCOUNTS AND DEFERRED REVENUE - Continued

Intergovernmental Receivables and Deferred Revenue

Intergovernmental receivables are primarily comprised of amounts due from the State and Federal governments. Revenue is recorded as earned when eligibility requirements are met. Grant revenues deferred in the governmental fund financial statements include unearned revenue and revenue received more than 60 days following year-end (unavailable to pay liabilities of the current period). Deferred revenue received after 60 days is fully recognized as revenue in the government-wide statements if grantor eligibility requirements are met.

Amounts due from other governments at June 30, 2008 are as follows:

| | |
|--------------------------------|--------------------|
| Due from the State of Michigan | |
| State aid | \$1,830,697 |
| Other State grants | 101,602 |
| Other | <u>542,048</u> |
| | <u>\$2,474,347</u> |

NOTE D - INVESTMENTS IN CAPITAL ASSETS

Investments in capital assets consist of the following:

| | Balance June 30, 2007 | Additions | Deletions | Balance June 30, 2008 |
|-------------------------------|--------------------------|--------------------|-------------|--------------------------|
| Site improvements | \$ 1,185,278 | \$ - | \$ - | \$ 1,185,278 |
| Buildings | 9,207,341 | - | - | 9,207,341 |
| Furniture and fixtures | 1,607,319 | 481,686 | - | 2,089,005 |
| Construction in progress | 10,013,956 | 5,700,502 | - | 15,714,458 |
| Buses and vehicles | <u>892,094</u> | <u>-</u> | <u>-</u> | <u>892,094</u> |
| Total | 22,905,988 | 6,182,188 | - | 29,088,176 |
| Less accumulated depreciation | (8,496,965) | (503,129) | - | (9,000,094) |
| Land | <u>250,768</u> | <u>-</u> | <u>-</u> | <u>250,768</u> |
| Total capital assets, net | <u>\$14,659,791</u> | <u>\$5,679,059</u> | <u>\$ -</u> | <u>\$20,338,850</u> |

Depreciation expense of \$503,129 was unallocated in the statement of activities.

NOTE E - STATE AID ANTICIPATION NOTE PAYABLE

The State aid anticipation note is secured by July and August State aid payments, bears interest at 3.44% and is due October 22, 2008.

NOTES TO FINANCIAL STATEMENTS - Continued

NOTE F - LONG-TERM LIABILITIES

Changes in long-term debt during the year ended June 30, 2008 were as follows:

| | Beginning Balance | New Debt | Payments/ Extinguishment | Ending Balance | Current Portion |
|-------------------------------|----------------------|-------------|-----------------------------|---------------------|--------------------|
| General obligation bonds | \$20,621,742 | \$ - | \$(630,000) | \$19,991,742 | \$727,538 |
| Unamortized refinancing costs | (344,205) | - | 30,104 | (314,101) | (30,104) |
| Unamortized bond premium | 692,796 | - | (52,100) | 640,696 | 52,100 |
| Accumulated leave liability | 293,979 | - | (9,436) | 284,543 | 22,838 |
| Termination benefits | <u>\$2,500</u> | - | <u>(52,500)</u> | - | - |
| Long-term debt June 30, 2008 | \$21,316,812 | \$ - | \$(713,932) | <u>\$20,602,880</u> | <u>\$772,372</u> |

Payments on general obligation bonds are made by the Debt Service Funds. The accumulated leave liability will be liquidated primarily from the General Fund.

At June 30, 2008, the School District's long-term debt consisted of the following:

| | |
|---------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|---------------------|
| 2005 Refunding Bonds ; due in annual installments of \$145,000 to \$570,000 through May 1, 2013; average interest rate of 3.85%. | \$ 2,610,000 |
| 2006 School Building and Site Bonds (QZAB) ; due in May 2020; no annual installments; 0% interest rate. | 3,401,764 |
| 1998 School Improvement Bonds (Durant) ; due in installments of \$3,884 to \$9,079 through May 15, 2013; average interest rate of 4.761353%. This debt will be repaid using revenues provided by the State of Michigan specifically for this purpose; should the State not provide these revenues, the School District is not liable for repayment of these bonds. | 79,978 |
| 2002 Energy Conservation Improvement Bonds ; due in annual installments of \$75,000 to \$150,000 through May 1, 2017; average interest rate of 3.5925%. | 1,110,000 |
| 2006 School Building and Site Bonds ; due in annual installments of \$50,000 to \$1,170,000 through May 1, 2026; average interest rate of 4.61776%. | <u>12,790,000</u> |
| Total general obligation bonds payable | 19,991,742 |
| Unamortized bond refinancing costs | (314,101) |
| Unamortized bond premium | 640,696 |
| Accumulated leave liability | <u>284,543</u> |
| Total long-term debt | <u>\$20,602,880</u> |

At the School District's option, bonds can be redeemed prior to maturity at a premium.

NOTES TO FINANCIAL STATEMENTS - Continued

NOTE F - LONG-TERM LIABILITIES - Continued

Total annual requirements to amortize bonds as of June 30, 2008 is as follows:

| Years Ending June 30, .. | <u>Principal</u> | <u>Interest</u> |
|-----------------------------|------------------|--------------------|
| 2009 | \$ 727,538 | \$ 741,580 |
| 2010 | 827,897 | 715,196 |
| 2011 | 863,273 | 684,645 |
| 2012 | 903,666 | 645,826 |
| 2013 | 987,604 | 626,240 |
| 2014-2018 | 4,255,000 | 2,477,612 |
| 2019-2023 | 8,066,764 | 1,462,563 |
| 2024-2026 | <u>3,360,000</u> | <u>312,250</u> |
| Totals | \$19,991,742 | <u>\$7,665,912</u> |

Interest expense for the year ended June 30, 2008 was \$734,363 and interest paid for the year ended June 30, 2008 was \$759,873.

Accumulated Leave Liability

Employees of the School District accumulate days of compensated sick leave, as specified by the bargaining units' contract. This benefit vests after one year of employment. Upon either resignation or retirement, the employees are compensated at daily rates specified in the bargaining units' contracts.

2006 School Building and Site Bonds (QZAB)

The 2006 School Building and Site Bonds are "qualified zone academy bonds" ("QZAB") under Section 1397E(d)(6) of the Internal Revenue Code, allowing holders of the bonds certain income tax credits. The QZAB bonds are due in May 2021 but require annual deposits of \$242,983 into an escrow account beginning May 2008. The escrow account balance was \$494,669 at June 30, 2008. The escrow deposits plus the interest earned thereon, which is fixed at 2.65%, will be sufficient to pay off the bonds upon maturity. Any spread from the escrow account will be paid to the purchaser of the bonds.

NOTE G - RISK MANAGEMENT

The School District is exposed to various risks of loss related to torts; theft of, damage to and destruction of assets; errors and omissions; injuries to employees; unemployment benefits; and natural disasters. The School District manages its risk exposures and provides certain employee benefits through a combination of self-insurance and risk management pools.

The School District pays unemployment claims on a reimbursement basis through the Bureau of Workers' and Unemployment Compensation ("BWUC"). As BWUC pays eligible recipients benefits, this amount is billed to Mason County Central School District. At June 30, 2008, there were no significant unbilled claims.

NOTES TO FINANCIAL STATEMENTS - Continued

NOTE G - RISK MANAGEMENT - Continued

The School District participates in SET-SEG's risk management pools for worker's compensation claims, liability insurance and errors and omissions coverages. SET-SEG was established pursuant to laws of the State of Michigan which authorize local units of government to jointly exercise any power, privilege or authority which each might exercise separately. The purpose of SET-SEG is to provide cooperative and comprehensive risk financing and risk control services. SET-SEG provides risk management, underwriting, reinsurance and claim review and processing services for all member governments pursuant to its charter.

The School District makes annual contributions to SET-SEG based on actuarial studies using historical data and insurance industry statistics. These contributions are paid from the General Fund. Such contributions as received by SET-SEG's General Fund are expended for reinsurance coverage, claim payments and certain general and administrative costs, whereas resources in the Member Retention Fund are used for loss payments and defense costs up to the member's self-insurance retention limits along with certain other member-specific costs. Any refunds from SET-SEG are deposited in the School District's General Fund.

NOTE H - BALANCES AND TRANSFERS/PAYMENTS WITHIN THE REPORTING ENTITY

Receivables and Payables

Outstanding balances between funds reported as "due to/from other funds" include outstanding charges by one fund to another for services or goods, subsidy commitments outstanding at year-end and other miscellaneous receivables/payables between funds.

| <u>Fund</u> | <u>Interfund Receivable</u> | <u>Interfund Payable</u> |
|--------------------------|---------------------------------|------------------------------|
| General Fund | \$ 16,738 | \$ - |
| Capital Projects A | - | 800 |
| Capital Projects B QZAB | 800 | - |
| Other governmental funds | 6,582 | 23,320 |
| | <u>\$ 24,120</u> | <u>\$ 24,120</u> |

Transfers and Payments

Transfers and payments within the reporting entity are substantially for the purposes of subsidizing operating functions, funding capital projects and asset acquisitions or maintaining debt service on a routine basis. Resources are accumulated in a fund to support and simplify the administration of various projects or programs.

The government-wide statement of activities eliminates transfers as reported within the segregated governmental activities columns. During the year ended June 30, 2008, the General Fund transferred payments of \$230,239 to the Athletic Fund and \$147,131 to the 2002 Debt Service Fund.

NOTES TO FINANCIAL STATEMENTS - Continued

NOTE I - PENSION PLAN

The School District contributes to the Michigan Public School Employees' Retirement Systems ("MPERS"), a cost-sharing multiple-employer defined benefit pension plan administered by the State of Michigan Department of Management & Budget Office of Retirement Services ("ORS"). MPERS provides retirement, disability, death and post-employment health benefits to plan members and beneficiaries. Member Investment Plan ("MIP") participants receive enhanced benefits compared to Basic Plan participants. Benefits are safeguarded by Article IX, Section 24 of the Michigan Constitution. Public Act 300 of 1980, as amended, assigns authority to establish and amend benefit provisions to the State Legislature. MPERS issues a publicly available financial report that includes financial statements and required supplementary information. That report may be obtained by writing to MPERS, PO Box 30171, Lansing, MI 48909, by calling (517) 322-5103, or on the State of Michigan's website @ www.michigan.gov.

Funding Policy

Plan members who participate in MIP are required to contribute 3.0% to 4.5% of their annual covered salary; plan members who participate in the Basic Plan may not contribute to the plan; and the School District is required to contribute at an actuarially determined rate using the individual entry age actuarial cost method. The rate was 17.74% for the period July 1, 2007 to September 30, 2007 and 16.72% for the period October 1, 2007 through June 30, 2008 of annual covered payroll. The contribution requirements of plan members and the School District are established and may be amended by the State Legislature. The School District's contributions to MPERS for the years ended June 30, 2008, 2007 and 2006 were \$1,352,141, \$1,425,189 and \$1,362,274, respectively, equal to the required contribution for each year.

Post-Employment Benefits

Under the MPERS Act, all retirees participating in the MPERS pension plan have the option of continuing health, dental and vision coverages. Retirees having these coverages contribute an amount equivalent to the monthly cost for Part B Medicare and 10% of the monthly premium amount for the health, dental and vision coverages. Required contributions for post-employment health care are included as part of the School District's total contribution to the MPERS plan discussed above.

NOTE J - COMMITMENTS AND CONTINGENCIES

Capital Projects

The Capital Projects Funds account for activity related to the construction of a new elementary school and renovation of existing facilities. Cumulative expenditures recognized for the construction period are \$17,240,713. The project is expected to be completed by June 30, 2009.

NOTES TO FINANCIAL STATEMENTS - Continued

NOTE J - COMMITMENTS AND CONTINGENCIES - Continued

Collectively Bargained Employment Agreements

The teachers of the School District are organized under the Mason County Central Education Association. The Board of Education and the Mason County Central Education Association had a contract for the year ended June 30, 2008. Under this agreement, the salary schedule allows for a 2.25% increase in salaries for all teachers at Steps 1 and above. Teachers also receive a longevity bonus at Steps 14, 19, 24 and 28, ranging from \$1,691 to \$7,329.

Federal and State Grants

In the normal course of operations, the School District receives grant funds from various Federal and State agencies. The grant programs are subject to audit by agents of the granting authorities, the purpose of which is to ensure compliance with conditions precedent to the granting of funds. Any liability for reimbursement which may arise as the result of these audits is not believed to be material.

REQUIRED SUPPLEMENTARY INFORMATION

Mason County Central School District

BUDGETARY COMPARISON SCHEDULE FOR THE GENERAL FUND

Year Ended June 30, 2008

| | Budgeted Amounts | | Actual (GAAP Basis) | Variances - Positive (Negative) | |
|------------------------------------------------------------------------|------------------|--------------|------------------------|---------------------------------|--------------------------|
| | Original | Final | | Original to Final | Final to Actual Total |
| Revenues | | | | | |
| Local and intermediate sources | \$ 1,954,363 | \$ 2,050,625 | \$ 2,044,222 | \$ 96,262 | \$ (6,403) |
| State revenues | 10,015,093 | 10,075,429 | 10,111,432 | 60,336 | 36,003 |
| Federal revenues | 681,618 | 705,026 | 653,432 | 23,408 | (51,594) |
| Incoming transfers and other transactions | 818,893 | 917,100 | 854,908 | 98,207 | (62,192) |
| Total revenues | 13,469,967 | 13,748,180 | 13,663,994 | 278,213 | (84,186) |
| Expenditures | | | | | |
| Current | | | | | |
| Instruction | 8,687,323 | 8,979,596 | 8,886,991 | (292,273) | 92,605 |
| Supporting Services | 4,375,740 | 4,421,434 | 4,410,305 | (45,694) | 11,129 |
| Total expenditures | 13,063,063 | 13,401,030 | 13,297,296 | (337,967) | 103,734 |
| REVENUES OVER (UNDER) EXPENDITURES | 406,904 | 347,150 | 366,698 | (59,754) | 19,548 |
| Other financing uses | | | | | |
| Operating transfers out | (390,706) | (378,881) | (377,370) | 11,825 | 1,511 |
| REVENUES OVER (UNDER) EXPENDITURES AND OTHER FINANCING USES | 16,198 | (31,731) | (10,672) | (47,929) | 21,059 |
| Fund balance, beginning of year | 273,596 | 273,596 | 273,596 | - | - |
| Fund balance, end of year | \$ 289,794 | \$ 241,865 | \$ 262,924 | \$ (47,929) | \$ 21,059 |

**COMBINING FINANCIAL STATEMENTS OF
NON-MAJOR GOVERNMENTAL FUNDS**

Mason County Central School District

COMBINING BALANCE SHEET - NON-MAJOR GOVERNMENTAL FUNDS

June 30, 2008

| | Special Revenue Funds | | Debt Service Funds | | | Total Non-Major Governmental Funds |
|---------------------------------------|-----------------------|-----------|--------------------|-----------|---------------------------|---------------------------------------------|
| | Food Service | Athletics | 1992 | 1997 | 2005 Refunding Bond | 2006 QZAB |
| ASSETS | | | | | | |
| Cash and cash equivalents | \$ - | \$ 1,045 | \$ 2,840 | \$ 32,140 | \$ 63,006 | \$ 24,177 |
| Due from other governments | 18,492 | - | - | - | - | - |
| Due from other funds | | 6,582 | | | | |
| Other receivables | 2,861 | - | - | - | - | - |
| Inventories - supplies and materials | 47,978 | - | - | - | - | - |
| Restricted cash | - | - | - | - | - | 952 |
| Restricted investments | - | - | - | - | - | 493,717 |
| Total assets | \$ 69,331 | \$ 7,627 | \$ 2,840 | \$ 32,140 | \$ 63,006 | \$ 518,846 |
| LIABILITIES | | | | | | |
| Accounts payable and accrued expenses | \$ 7,078 | \$ 7,627 | \$ - | \$ - | \$ - | \$ - |
| Due to other funds | 23,320 | - | - | - | - | - |
| Total liabilities | 30,398 | 7,627 | - | - | - | - |
| FUND BALANCES | | | | | | |
| Reserved for debt service | - | - | 2,840 | 32,140 | 63,006 | 518,846 |
| Reserved for inventories | 38,933 | - | - | - | - | - |
| Total fund balances | 38,933 | - | 2,840 | 32,140 | 63,006 | 518,846 |
| Total liabilities and fund balances | \$ 69,331 | \$ 7,627 | \$ 2,840 | \$ 32,140 | \$ 63,006 | \$ 518,846 |
| | | | | | | \$ 1,021,105 |

Mason County Central School District

COMBINING STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES - NON-MAJOR GOVERNMENTAL FUNDS

Year Ended June 30, 2008

| | Special Revenue Funds | | Debt Service Funds | | | 2005 | 2006 QZAB | Total Non-Major Governmental Funds |
|---------------------------------|-----------------------|------------------|--------------------|---------------|------------------|-------------------|----------------|---------------------------------------------|
| | Food Service | Athletic | 1992 | 1997 | 2002 | Refunding Bond | 2006 | |
| Revenues | | | | | | | | |
| Property taxes | \$ - | \$ - | \$ - | \$ 75 | \$ - | \$ 601,616 | \$ 648,018 | \$ 1,491,173 |
| Interest | 782 | - | 87 | 977 | - | 3,648 | 6,760 | 22,644 |
| State revenues | 31,437 | - | - | - | - | - | - | 31,437 |
| Federal revenues | 318,989 | - | - | - | - | - | - | 318,989 |
| Other | 334,351 | 55,482 | - | - | - | - | - | 389,833 |
| Total revenues | 685,559 | 55,482 | 87 | 1,052 | - | 605,264 | 654,778 | 2,254,076 |
| Expenditures | | | | | | | | |
| Food Service | 703,274 | - | - | - | - | - | - | 703,274 |
| Athletics | - | 285,721 | - | - | - | - | - | 285,721 |
| Debt Service | | | | | | | | |
| Principal | - | - | - | - | 95,000 | 485,000 | 50,000 | 630,000 |
| Interest | - | - | - | - | 52,131 | 117,313 | 590,429 | 759,873 |
| Other | - | - | - | - | - | 450 | - | 850 |
| Total expenditures | 703,274 | 285,721 | - | - | 147,131 | 602,763 | 640,429 | 2,379,718 |
| REVENUES OVER (UNDER) | (17,715) | (230,239) | 87 | 1,052 | (147,131) | 2,501 | 14,349 | (125,642) |
| Other financing sources | | | | | | | | |
| Operating transfers in | - | 230,239 | - | - | 147,131 | - | - | 377,370 |
| REVENUES OVER (UNDER) | | | | | | | | |
| EXPENDITURES AND OTHER | (17,715) | - | 87 | 1,052 | - | 2,501 | 14,349 | 251,728 |
| FINANCING SOURCES | 56,648 | - | 2,753 | 31,088 | - | 60,505 | 312,966 | 731,352 |
| Fund balance, beginning of year | | | | | | | | |
| Fund balance, end of year | \$ 38,933 | \$ - | \$ 2,840 | \$ 32,140 | \$ - | \$ 63,006 | \$ 327,315 | \$ 983,080 |

FEDERAL PROGRAMS

Mason County Central School District

SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

Year Ended June 30, 2008

| Federal Grantor/ Pass Through Grantor Program Title | Pass-Through Grantor's Number | Federal CFDA Number | Original Approved Award/Grant Amount | Receivable July 1, 2007 | Prior Year Expenditures | Current Year Receipts/ Revenue Recognized | Current Year Expenditures | Receivable June 30, 2008 |
|---------------------------------------------------------------------------------------|-------------------------------------|---------------------------|-----------------------------------------------|----------------------------|----------------------------|----------------------------------------------------|---------------------------------|-----------------------------|
| United States Department of Education Passed through State Department of Education | | | | | | | | |
| E.S.E.A. Title I | | | | | | | | |
| | 81530-0708 | 84.010 | \$ 276,277 | \$ - | \$ - | \$ 216,028 | \$ 273,454 | \$ 57,426 |
| | 71530-0607 | | 246,074 | 43,053 | 246,074 | 43,053 | - | - |
| E.S.E.A. Title I Summer Migrant | 71830-2007 | | 80,088 | 24,277 | 24,277 | 80,088 | 55,811 | - |
| | | | 602,439 | 67,330 | 270,351 | 339,169 | 329,265 | 57,426 |
| E.S.E.A. Title I Summer Migrant Migrant Regular Development | 81830-2008 | 84.011 | 91,191 | - | - | 4,528 | 27,055 | 22,527 |
| | 71890-0607 | | 43,077 | 11,486 | 43,077 | 11,486 | - | - |
| | 81890-0708 | | 38,513 | - | - | 38,513 | 38,513 | - |
| | | | 172,781 | 11,486 | 43,077 | 54,527 | 65,568 | 22,527 |
| E.S.E.A. Title V | 80250-0708 | 84.298 | 1,914 | - | - | 1,914 | 1,914 | - |
| Tech Fit Challenge | 74290-0607 | 84.318 | 2,526 | 211 | 2,526 | 211 | - | - |
| | 84290-0708 | | 2,597 | - | - | 2,597 | 2,597 | - |
| | | | 5,123 | 211 | 2,526 | 2,808 | 2,597 | - |
| Service Provider Self Review | 80440-0708 | 84.027 | 4,000 | - | - | 4,000 | 4,000 | - |
| Drug Free Schools | 72860-0708 | 84.186 | 1,558 | - | - | 1,558 | 1,558 | - |
| | 082860-0708 | | 7,226 | - | - | 5,710 | 6,061 | 351 |
| | 72860-0506 | | 5,244 | 1,576 | 5,244 | 1,576 | - | - |
| | | | 14,028 | 1,576 | 5,244 | 8,844 | 7,619 | 351 |
| Homeless Children & Youth | 82320-0708 | 84.196 | 19,639 | - | - | 12,000 | 12,818 | 818 |
| | 72320-0607 | | 11,553 | 5,337 | 11,033 | 5,857 | 520 | - |
| | | | 31,192 | 5,337 | 11,033 | 17,857 | 13,338 | 818 |
| Teacher Quality Title IIA | 60520-0506 | 84.367 | 93,679 | - | - | 73,199 | 93,679 | 20,480 |
| | 70520-0607 | | 92,831 | 10,319 | 92,831 | 10,319 | - | - |
| | | | 186,510 | 10,319 | 92,831 | 83,518 | 93,679 | 20,480 |
| Total pass through United States Department of Education | | | 1,017,987 | 96,259 | 425,062 | 512,637 | 517,980 | 101,602 |

The accompanying notes are an integral part of this financial schedule.

Mason County Central School District
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
Year Ended June 30, 2008

| Federal Grantor/ Pass Through Grantor Program Title | Pass-Through Grantor's Number | Federal CFDA Number | Original Award/Grant Amount | Receivable July 1, 2007 | Prior Year Expenditures | Current Year Receipts/ Revenue Recognized | Current Year Expenditures | Receivable June 30, 2008 |
|--------------------------------------------------------------------|-------------------------------------|---------------------------|-----------------------------------|----------------------------|----------------------------|----------------------------------------------------|---------------------------------|-----------------------------|
| United States Department of Agriculture | | | | | | | | |
| Child Nutrition Cluster | | | | | | | | |
| Passed through State Department of Education | | | | | | | | |
| National School Lunch | 71950 | 10.555 | \$ 36,523 | \$ 30 | \$ 32,727 | \$ 3,827 | \$ 3,797 | \$ - |
| | 71960 | | 200,363 | 60 | 179,222 | 21,201 | 21,141 | - |
| | 81950 | | 33,562 | - | - | 33,562 | 33,562 | - |
| | 81960 | | 189,444 | - | - | 189,444 | 189,444 | - |
| National School Lunch - Breakfast | 71970 | 10.553 | 59,028 | 3 | 53,714 | 5,314 | 5,311 | - |
| | 81970 | | 50,518 | - | - | 50,518 | 50,518 | - |
| Summer Feeding Program | 70900 | 10.559 | 16,804 | - | - | 16,804 | 16,804 | - |
| | 71900 | | 1,751 | - | - | 1,751 | 1,751 | - |
| Entitlement Commodities | | 10.550 | 14,840 | - | - | 14,840 | 14,840 | - |
| Bonus Commodities | | | 377 | - | - | 377 | 377 | - |
| Total United States Department of Agriculture | | | 603,210 | 93 | 265,663 | 337,638 | 337,545 | - |
| United States Department of Health and Human Services | | | | | | | | |
| Passed through Area Agency on Aging of West Michigan, Inc. | | | | | | | | |
| Aging Cluster: | | | | | | | | |
| Title III B 06/07 | | 93.044 | 16,601 | 1,330 | 16,601 | 1,330 | - | - |
| Title III E 06/07 | 61.7 | | 21,566 | 4,153 | 21,566 | 4,153 | - | - |
| Title III B 07/08 | | | 16,601 | - | - | 12,796 | 14,915 | 2,119 |
| Title III E 07/08 | | | 18,566 | - | - | 10,430 | 16,409 | 5,979 |
| Title III C1 07/08 | | 93.045 | 14,720 | - | - | 9,084 | 11,367 | 2,283 |
| Title III C1 06/07 | 61.7 | | 13,755 | 2,660 | 10,205 | 6,210 | 3,550 | - |
| Title III C2 07/08 | | | 31,733 | - | - | 15,976 | 24,312 | 8,336 |
| Title III C2 06/07 | 61.7 | | 29,848 | 7,666 | 22,828 | 14,686 | 7,020 | - |
| USDA-07/08 | | 93.053 | 26,474 | - | - | 18,090 | 21,855 | 3,765 |
| USDA-06/07 | | | 28,377 | 4,687 | 20,113 | 12,951 | 8,264 | - |
| Total United States Department of Health and Human Services | | | 218,241 | 20,496 | 91,313 | 105,706 | 107,692 | 22,482 |
| Total | | | \$ 1,839,438 | \$ 116,848 | \$ 782,038 | \$ 955,981 | \$ 963,217 | \$ 124,084 |

Mason County Central School District

NOTES TO SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

June 30, 2008

- Note 1** The Schedule of Expenditures of Federal Awards is prepared on the accrual basis of accounting.
- Note 2** Management has reported that expenditures in this Schedule of Expenditures of Federal Awards are equal to those amounts reported in the annual or final cost reports. Unallowed differences, if any, have been disclosed to the auditor.
- Note 3** The financial reports, including claims for advances and reimbursements and amounts claimed or used for matching are timely, complete, accurate and contain information that is supported by the books and records from which the basic financial statements have been prepared. Grant receipts reported on the Schedule of Expenditures of Federal Awards, as passed through the Michigan Department of Education, reconcile to the Grant Section Auditor's Report (R7120). Unreconciled differences have been disclosed to the auditor.
- Note 4** A reconciliation of expenditures on the Schedule of Expenditures of Federal Awards' sources on the financial statements is as follows:

| | |
|------------------------------------------|------------------|
| Federal expenditures per Schedule of | |
| Expenditures of Federal Awards | \$963,217 |
| Timing differences | <u>9,204</u> |
| Federal sources per financial statements | <u>\$972,421</u> |

**REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING
AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT
OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH
GOVERNMENT AUDITING STANDARDS**

Board of Education
Mason County Central School District

We have audited the financial statements of the governmental activities, each major fund and the aggregate remaining fund information of Mason County Central School District (the "School District") as of and for the year ended June 30, 2008, which collectively comprise the School District's basic financial statements and have issued our report thereon dated September 19, 2008. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the School District's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the School District's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the School District's internal control over financial reporting.

Our consideration of internal control was for the limited purpose described in the preceding paragraph and would not necessarily identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses. However, as discussed below, we identified certain deficiencies in internal control over financial reporting that we consider to be significant deficiencies.

A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the School District's ability to initiate, authorize, record, process or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the School District's financial statements that is more than inconsequential will not be prevented or detected by the School District's internal control. We consider the deficiencies described in the accompanying Schedule of Findings and Questioned Costs, as finding 2008-1 and 2008-2, to be significant deficiencies in internal control over financial reporting.

Member of



415 Munson Avenue, Post Office Box 947
Traverse City, Michigan 49685-0947
231.946.1792, FAX: 231.946.2762
www.dgnpcpa.com

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the School District's internal control.

Our consideration of the internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in the internal control that might be significant deficiencies and, accordingly, would not necessarily disclose all significant deficiencies that are also considered to be material weaknesses. However, we believe that both the significant deficiencies described above are material weaknesses.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the School District's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under Government Auditing Standards.

The School District's response to the findings identified in our audit is described in the accompanying Schedule of Findings and Questioned Costs. We did not audit the School District's response and, accordingly, we express no opinion on it.

This report is intended solely for the information and use of the audit committee, the Board of Education, management, Michigan Department of Education, Federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

Dennis Gortland & Niergarth

September 19, 2008

**REPORT OF COMPLIANCE WITH REQUIREMENTS APPLICABLE
TO EACH MAJOR PROGRAM AND INTERNAL CONTROL OVER
COMPLIANCE IN ACCORDANCE WITH OMB CIRCULAR A-133**

Board of Education
Mason County Central School District

Compliance

We have audited the compliance of Mason County Central School District (the "School District") with the types of compliance requirements described in the U.S. Office of Management and Budget ("OMB") Circular A-133 *Compliance Supplement* that are applicable to each of its major Federal programs for the year ended June 30, 2008. The School District's major Federal programs are identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs. Compliance with the requirements of laws, regulations, contracts and grants applicable to each of its major Federal programs is the responsibility of the School District's management. Our responsibility is to express an opinion on the School District's compliance based on our audit.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB Circular A-133, *Audits of States, Local Governments and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major Federal program occurred. An audit includes examining, on a test basis, evidence about the School District's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination on the School District's compliance with those requirements.

In our opinion, the Mason County Central School District complied, in all material respects, with the requirements referred to above that are applicable to each of its major Federal programs for the year ended June 30, 2008.

Member of



415 Munson Avenue, Post Office Box 947
Traverse City, Michigan 49685-0947
931.946.1199, FAX: 931.946.9769
www.dgncpa.com

Internal Control Over Compliance

The management of the School District is responsible for establishing and maintaining effective internal control over compliance with requirements of laws, regulations, contracts and grants applicable to Federal programs. In planning and performing our audit, we considered the School District's internal control over compliance with the requirements that could have a direct and material effect on a major Federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of School District's internal control over compliance.

A control deficiency in an entity's internal control over compliance exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect noncompliance with a type of compliance requirement of a Federal program on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the entity's ability to administer a Federal program such that there is more than a remote likelihood that noncompliance with a type of compliance requirement of a Federal program that is more than inconsequential will not be prevented or detected by the entity's internal control.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that material noncompliance with a type of compliance requirement of a Federal program will not be prevented or detected by the entity's internal control.

Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in internal control that might be significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses, as defined above.

This report is intended solely for the information and use of the audit committee, Board of Education, management, Michigan Department of Education, Federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

Dennis. Gartland & Niergarth

September 19, 2008

Mason County Central School District
SCHEDULE OF FINDINGS AND QUESTIONED COSTS

June 30, 2008

Prior Year

Findings in Accordance with Governmental Auditing Standards

Finding Number 2007-1

Criteria: All Michigan school districts are required to prepare financial statements in accordance with generally accepted accounting principles ("GAAP"). This is a responsibility of the School District's management. The preparation of financial statements in accordance with GAAP requires internal controls over both (1) recording, processing and summarizing accounting data (i.e., maintaining internal books and records), and (2) reporting government-wide and fund financial statements, including the related footnotes (i.e., external financial reporting.)

Condition: As is the case with many smaller and medium-sized entities, the School District has at times relied on its independent external auditors to assist in the preparation of the government-wide financial statements and footnotes as part of its external financial reporting process. Accordingly, the School District's ability to prepare financial statements in accordance with GAAP is based, in part, on its reliance on its external auditors, who cannot by definition be considered a part of the School District's internal controls.

Cause: This condition was caused by the School District's decision that it is more cost effective to work with the external auditors for assistance in the preparation of its annual financial statements than to incur the time and expense of obtaining the necessary training and tools required for the School District to perform this task internally.

Effect: As a result of this condition, the School District lacks internal controls over the preparation of financial statements in accordance with GAAP and instead relies, in part, on its external auditors for assistance with this task.

Management's Response: The School District has evaluated the cost vs. benefit of establishing internal controls over the preparation of financial statements in accordance with GAAP, and determined that it is in the best interests of the School District to work with its external auditors and to carefully review the draft financial statements and notes prior to approving them and accepting responsibility for their content and presentation.

Current Status: The finding is repeated for the year ended June 30, 2008.

Mason County Central School District

SCHEDULE OF FINDINGS AND QUESTIONED COSTS - Continued

June 30, 2008

Findings in Accordance with Governmental Auditing Standards - Continued

Finding Number 2007-2

Criteria: Adequate segregation of duties for the School District is necessary to minimize the likelihood that fraud or errors could occur and not be detected.

Condition: The School District has not achieved a complete segregation of duties among employees who have both access to assets and accounting responsibilities.

Cause: The small size of the business office staff creates an inherent lack of segregation of duties.

Effect: As a result of this condition, the School District lacks proper segregation of duties and is exposed to an increased risk of misstatement of its financial statements.

Management's Response: The School District has evaluated the manner in which they segregate duties and has implemented certain measures. However, the cost associated with adding additional staff to achieve a complete segregation is not justified by the expected benefits.

Current Status: The finding is repeated for the year ended June 30, 2008.

Current Year

Section 1 - Summary of Auditor's Results

1. The audit report on Mason County Central School District's financial statements was unqualified.
2. There were two significant deficiencies in internal control, which constitute material weaknesses, reported as a result of the audit of the financial statements. See Section 2 - Findings in Accordance with Governmental Auditing Standards.
3. There were no compliance findings disclosed that were material to the School District's financial statements.
4. There were no significant deficiencies disclosed that were related to a major program.
5. The report over compliance for major programs was unqualified.
6. There were no audit findings that are required to be reported in accordance with Section 510(a) of OMB Circular A-133.

Mason County Central School District

SCHEDULE OF FINDINGS AND QUESTIONED COSTS - Continued

June 30, 2008

7. The School District's major programs are Child Nutrition Cluster (10.553, 10.555 and 10.559) and Title I (84.010).
8. The dollar threshold for distinguishing between Type A and Type B programs was \$300,000.
9. The auditee did not qualify as low risk auditee.

Section 2 - Findings in Accordance with Governmental Auditing Standards

Finding Number 2008-1

Criteria: All Michigan school districts are required to prepare financial statements in accordance with generally accepted accounting principles ("GAAP"). This is a responsibility of the School District's management. The preparation of financial statements in accordance with GAAP requires internal controls over both (1) recording, processing and summarizing accounting data (i.e., maintaining internal books and records), and (2) reporting government-wide and fund financial statements, including the related footnotes (i.e., external financial reporting.)

Condition: As is the case with many smaller and medium-sized entities, the School District has at times relied on its independent external auditors to assist in the preparation of the government-wide financial statements and footnotes as part of its external financial reporting process. Accordingly, the School District's ability to prepare financial statements in accordance with GAAP is based, in part, on its reliance on its external auditors, who cannot by definition be considered a part of the School District's internal controls.

Cause: This condition was caused by the School District's decision that it is more cost effective to work with the external auditors for assistance in the preparation of its annual financial statements than to incur the time and expense of obtaining the necessary training and tools required for the School District to perform this task internally.

Effect: As a result of this condition, the School District lacks internal controls over the preparation of financial statements in accordance with GAAP and instead relies, in part, on its external auditors for assistance with this task.

Management's Response: The School District has evaluated the cost vs. benefit of establishing internal controls over the preparation of financial statements in accordance with GAAP, and determined that it is in the best interests of the School District to work with its external auditors and to carefully review the draft financial statements and notes prior to approving them and accepting responsibility for their content and presentation.

SCHEDULE OF FINDINGS AND QUESTIONED COSTS - Continued

Section 2 - Findings in Accordance with Governmental Auditing Standards - Continued

Finding Number 2008-2

Criteria: Adequate segregation of duties for the School District is necessary to minimize the likelihood that fraud or errors could occur and not be detected.

Condition: The School District has not achieved a complete segregation of duties among employees who have both access to assets and accounting responsibilities.

Cause: The small size of the business office staff creates an inherent lack of segregation of duties.

Effect: As a result of this condition, the School District lacks proper segregation of duties and is exposed to an increased risk of misstatement of its financial statements.

Management's Response: The School District has evaluated the manner in which they segregate duties and has implemented certain measures. However, the cost associated with adding additional staff to achieve a complete segregation is not justified by the expected benefits.

Section 3 - Current Year Findings and Questioned Costs in Accordance with OMB Circular A-133

No findings.



Business and Financial Advisors
Our clients' success – our business

Thomas E. Gartland, CPA
Brad R. Niergarth, CPA
James G. Shumate, CPA
Robert C. Thompson, CPA
Michael D. Shew, CPA
Mary F. Krantz, CPA
Shelly K. Bedford, CPA
Heidi M. Wendel, CPA

AUDIT-RELATED COMMUNICATIONS

To the Board of Education
Mason County Central School District

We have audited the financial statements of the governmental activities, each major fund and the aggregate remaining fund information of Mason County Central School District (the "School District") for the year ended June 30, 2008 and have issued our report thereon dated September 19, 2008. Professional standards require that we provide you with the following information related to our audit.

Our Responsibility under U.S. Generally Accepted Auditing Standards and OMB Circular A-133

As stated in our engagement letter dated August 11, 2008, our responsibility, as described by professional standards, is to express opinions about whether the financial statements prepared by management with your oversight are fairly presented, in all material respects, in conformity with U.S. generally accepted accounting principles. Our audit of the financial statements does not relieve you or management of your responsibilities.

Our responsibility is to plan and perform the audit to obtain reasonable, but not absolute, assurance that the financial statements are free of material misstatement.

We are responsible for communicating significant matters related to the audit that are, in our professional judgment, relevant to your responsibilities in overseeing the financial reporting process. However, we are not required to design procedures specifically to identify such matters.

Compliance

As part of obtaining reasonable assurance about whether the School District's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grants, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit.



415 Munson Avenue, Post Office Box 947
Traverse City, Michigan 49685-0947
231.946.1722, FAX: 231.946.2762
www.dsnrcpa.com

Also, in accordance with OMB Circular A-133, we examined, on a test basis, evidence about the School District's compliance with the types of compliance requirements described in the U.S. Office of Management and Budget ("OMB") Circular A-133 Compliance Supplement applicable to each of its major Federal programs for the purpose of expressing an opinion on the School District's compliance with those requirements. While our audit provides a reasonable basis for our opinion, it does not provide a legal determination on the School District's compliance with those requirements.

Internal Controls

In planning and performing our audit, we considered the School District's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinions on the financial statements and not to provide assurance on the internal control over financial reporting. We also considered internal control over compliance with requirements that could have a direct and material effect on a major Federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with OMB Circular A-133.

Our consideration of internal control was for the limited purpose described in the preceding paragraph and would not necessarily identify all deficiencies in internal control that might be significant deficiencies or material weaknesses. However, as discussed below, we identified certain deficiencies in internal control that we consider to be significant deficiencies or material weaknesses.

A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A *significant deficiency* is a control deficiency, or a combination of control deficiencies, that adversely affects the School District's ability to initiate, authorize, record, process or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the School District's financial statements that is more than inconsequential will not be prevented or detected by the School District's internal control.

A material weakness is a significant deficiency, or a combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the School District's internal control.

We consider the following deficiencies to be significant deficiencies in internal control:

Reporting Financial Data (Finding Number 2008-1)

The above definition of a significant deficiency includes any condition that adversely affects the School District's ability to report financial data in accordance with GAAP. As a matter of convenience, the School District has always relied upon its auditors to prepare financial statements and related notes and supplemental schedules for external reporting in accordance with GAAP. As a consequence, the School District has not developed the tools and resources necessary to enable its employees to prepare reports in conformity with GAAP in the normal course of performing their assigned functions. The School District has committed the resources necessary to meet its internal reporting needs. In this regard, the School District is not unlike many other schools of its size and nature.

Segregation of Duties (Finding Number 2008-2)

The size of the administrative staff precludes proper segregation of duties for optimal internal control. Ideally, the internal control system of the School District should segregate the accounting responsibilities from employees who have access to physical assets such as cash, investments and payroll from authorization and approval of transactions and account reconciliations. Although there is no indication of any significant errors or misappropriation of assets, the Board must be aware of the lack of segregation of duties.

Planned Scope and Timing of the Audit

We performed the audit according to the planned scope and timing previously communicated to you in our letter about planning matters on August 22, 2008.

Qualitative Aspects of Accounting Practices

Management is responsible for the selection and use of appropriate accounting policies. The significant accounting policies used by Mason County Central School District are described in Note A to the financial statements. No new accounting policies were adopted and the application of existing policies was not changed during 2008. We noted no transactions entered into by the School District during the year for which there is a lack of authoritative guidance or consensus. There are no significant transactions that have been recognized in the financial statement in a different period than when the transaction occurred.

Accounting estimates are an integral part of the financial statements prepared by management and are based on management's knowledge and experience about past and current events and assumptions about future events. Certain accounting estimates are particularly sensitive because of their significance to the financial statements and because of the possibility that future events affecting them may differ significantly from those expected. However, none of management's estimates are considered to be particularly sensitive.

No Difficulties Encountered in Performing the Audit

We encountered no significant difficulties in dealing with management in performing and completing our audit.

Corrected and Uncorrected Misstatements

Professional standards require us to accumulate all known and likely misstatements identified during the audit, other than those that are trivial, and communicate them to the appropriate level of management. Management has corrected all such misstatements. In addition, none of the misstatement detected as a result of audit procedures and corrected by management were material, either individually or in the aggregate, to the financial statements taken as a whole.

No Disagreements with Management

For purposes of this letter, professional standards define a disagreement with management as a financial accounting, reporting or auditing matter, whether or not resolved to our satisfaction, that could be significant to the financial statements or the auditor's report. We are pleased to report that no such disagreements arose during the course of our audit.

Management Representations

We have requested certain representations from management that are included in the management representation letter dated September 19, 2008.

Management Consultations with Other Independent Accountants

In some cases, management may decide to consult with other accountants about auditing and accounting matters, similar to obtaining a "second opinion" on certain situations. If a consultation involves application of an accounting principle to the governmental unit's financial statements or a determination of the type of auditor's opinion that may be expressed on those statements, our professional standards require the consulting accountant to check with us to determine that the consultant has all the relevant facts. To our knowledge, there were no such consultations with other accountants.

Other Audit Findings or Issues

We generally discuss a variety of matters, including the application of accounting principles and auditing standards, with management each year prior to retention as the Mason County Central School District's auditors. However, these discussions occurred in the normal course of our professional relationship and our responses were not a condition to our retention.

General Comments and Considerations

Budget Fund Balance

State law mandates that school districts do not operate with a deficit budget. State law does not, however, mandate maintaining a healthy fund balance. Maintaining a minimum fund balance is only smart management of the school district's resources. We believe a fund balance of approximately 15% of the total annual operation expense of the school district's General Fund budget is a good target fund balance. The current fund balance is \$262,924, approximately 2% of the annual operating expenses. Setting a target fund balance to maintain would provide flexibility in dealing with unanticipated budget emergencies such as mid-year reductions in State funding. We recommend the School District discuss a target fund balance and adopt a Board policy. This will provide guidance and direction on an annual basis as each year's operating budget is prepared and adopted.

Headlee Rollback

Under Proposal A, school districts receive a foundation allowance multiplied by the number of students. The foundation allowance is paid from two sources, property taxes and the State. The 18 mills approved by voters in 1996 for non-homestead property is the portion determined to come from property taxes. When property is sold and re-valued at a level much higher than the rate of inflation, it can cause the 18 mills to be rolled back. This is the case with Mason County Central School District. This reduction approximated \$130,000 in 2008. The State does not pick up this difference in reduction of mills. To get the full per student operational dollars that the State authorized under Proposal A, school districts may find it necessary to hold an override vote to restore the full 18 mills. Headlee rollback reduces the authorized millage rate, not the levied rate. So, school districts with high growth may find it necessary to hold an override vote annually if only the 18 mills are requested. Such school districts might find it appropriate to request authorization of 20 to 21 mills. Since State law prohibits school districts from levying more than 18 mills, there is no downside to authorizing more than the needed 18 mills. Then, if a rollback occurs, it is applied to the 20 or 21 mills, not the 18 mills levied. This would eliminate the need to come back again and again to voters to ask for the same 18 mill levy.

This information is intended solely for the use of the Board of Education and management of Mason County Central School District and is not intended to be and should not be used by anyone other than these specified parties.

We are pleased to serve as the School District's auditors. If there are any questions about the audited financial statements or the contents of this letter, we would welcome the opportunity to discuss them at your convenience.

Dennis, Gartland & Niergarth

September 19, 2008